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No. 239

In the Supreme Court of the United States

October Term, 1935

Guy T. Helvering, Commissioner of Internal

E. B. Crocker and Edward Dickey, Executors of
the Estate of Mary Wolf, No. 2, Deceased

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES CIRCUIT COURT OF APPEALS FOR THE NINTH
CIRCUIT

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In the Supreme Court of the United States

OCTOBER TERM, 1935

No. ——

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

E. E. COMBS AND EDWARD EVERETT, TRUSTEES OF E. E. Combs Well No. 2, Express Trust

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Ninth Circuit entered in the above-entitled cause on April 11, 1935.

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 20–26) is unreported. The opinion of the Circuit Court of Appeals is reported in 76 F. (2d) 682.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered April 11, 1935. The jurisdiction of

this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the trust here involved was an association and as such taxable as a corporation.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1926, c. 27, 44 Stat. 9:

> SEC. 2. (a) When used in this Act—
>
> * * * * * *
>
> (2) The term "corporation" includes associations, joint-stock companies, and insurance companies.
>
> (U. S. C. App., Title 26, Sec. 1262.)

Treasury Regulations 69, promulgated under the Revenue Act of 1926:

> ART. 1502. *Associations.* — Associations and joint-stock companies include associations, common law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the shareholders on the basis of the capital stock which each holds, or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the organization. * * *

ART. 1504. *Association distinguished from trust.*—Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries in the carrying on of any business, and the beneficiaries have no control over the trust, although their consent may be required for the filling of a vacancy among the trustees or for a modification of the terms of the trust, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by section 219 and by articles 341–347. If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of section 2. Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute.

STATEMENT

The facts were stipulated (R. 34–43) and may be summarized as follows:

The trust here involved was created by a "Memorandum of Formation of Express Trust" (R. 36–

41), executed on February 6, 1925. The purpose as stated therein was to finance and drill a well for the production and sale of oil and other hydrocarbon substances under an oil and gas lease dated July 24, 1924. This instrument was signed by the Hub Oil Company, as assignor, and by E. E. Combs and Edward Everett, as trustees. It stated that there was assigned to the trustees all rights of a lessee under the lease subject to a reservation to the assignor of 6.5% of all oil, gas and other hydrocarbons produced, and subject also to a reserved royalty of 2% to another person. The assignor agreed to supply certain drilling equipment at its fair market value, and one Sheridan Bailes agreed to furnish other equipment and to superintend all drilling and production operations for a consideration of 12% of the production. The trust was to pay all labor claims and for materials not supplied by the Hub Oil Company or by Bailes. (R. 37–38.)

The "whole beneficial interest" in the trust was to be 71⅓% of the gross production of the well. This interest was to be owned as follows: (1) 25% less certain deductions for trust obligations to beneficiaries providing money for trust purposes, (2) 44⅓% to E. E. Combs less like deductions, and (3) 2% to Edward Everett also less such deductions. The agreement provided for the issuance of certificates of beneficial interest transferable only upon the books of the trust when endorsed and surrendered. (R. 40–41, 43.)

The trustees were given the following powers and duties: (1) To hold all property, the legal title to which might vest in them under the trust, (2) to use all monies which were to be deposited by the beneficiaries to pay for labor and materials incident to the drilling and producing operations, (3) to exercise all the rights of a lessee under the lease except as otherwise provided, (4) to pay the trust debts, (5) to manage and protect the trust property, (6) to sell and contract for the sale of all products of the well, (7) to loan and borrow money upon the credit of the trust for trust purposes, and (8) to sell any remaining beneficial interest in the trust as they might deem best for trust purposes. Combs was also to act as Production Manager when the well started producing. (R. 38–39.)

The trust agreement also provided that the beneficial interests of E. E. Combs could be sold by the trustees for the purpose of raising funds to pay the expenses incident to producing oil from one well and not otherwise provided for from funds to be deposited by the beneficiaries, and that no portion of any royalties accruing to the beneficiaries should be used for the payment of any such expenses until the beneficial interests of E. E. Combs were exhausted. (R. 39–40.)

The provisions of the trust agreement were carried out and the Hub Oil Company received $15,000 out of the proceeds of the oil. Sheridan Bailes received 12% of the production as agreed. (R. 35.)

Thirteen persons contributed a total of $25,000 (R. 42) and received certificates entitling them to 25% of the net production of the well. E. E. Combs sold 9¼% of the net production of the well, which had been assigned to him, for $9,250 and spent all of the money received in drilling operations. (R. 35.)

A well was drilled in 1925 and produced oil throughout the remainder of that year and during 1926 until the trustees sold the lease. The trustees distributed the amount received from the sale of the lease to the beneficiaries and had also currently distributed, during 1925 and 1926, the amounts received from the sale of oil. After the lease was sold and the proceeds distributed, the trust was terminated. (R. 35.)

During its existence the trust had no office or place of business, no seal, no by-laws, and no official name. The trustees acquired only the one lease, and did not borrow any money or engage in any other business. During such time the beneficiaries held no meetings. (R. 35–36.)

The Commissioner held that the trust was an association taxable as a corporation and determined deficiencies in income taxes for the years 1925 and 1926 in the amounts of $2,741.95 and $4,627.27, respectively. (R. 8.) The Board of Tax Appeals decided that the trust was not so taxable and its decision was affirmed by the Circuit Court of Appeals.

SPECIFICATION OF ERROR TO BE URGED

The Circuit Court of Appeals erred in holding that the trust was not taxable as an association.

REASONS FOR GRANTING THE WRIT

1. The question presented here is one about which there is much confusion and as it is involved in many cases now pending in the courts and in the Bureau of Internal Revenue, it is a question of general importance. In deciding the instant case the Circuit Court of Appeals called attention to the frequency with which this question has been presented to the courts and stated it is a close one and not free from difficulty. A similar view was recently taken in *Coleman-Gilbert Associates* v. *Commissioner*, 76 F. (2d) 191 (C. C. A. 1st), in which the court there stated that (p. 193):

> There are numerous decisions of the Board of Tax Appeals and Circuit Courts of Appeals in review, without laying down any definite line of demarkation between an association and a pure trust. * * * In any event, *the decisions are seemingly in a hopeless state of confusion.* * * * (Italics supplied.)

The existing confusion in these cases extends not only to decisions by courts of different circuits but to decisions by the same courts. For instance, the decision in the instant case is not consistent with the earlier decision by the Circuit Court of Appeals for the Ninth Circuit in *Morrissey* v. *Commissioner*,

74 F. (2d) 803. The taxpayer's petition for certiorari in the *Morrissey* case was granted on May 13, 1935, No. 17, October Term, 1935.

A petition for certiorari was filed on behalf of the Commissioner in the case of *Coleman Gilbert Associates, supra,* on May 27, 1935, Nos. 78 and 79, October Term, 1935.

2. The decision in the instant case is in substantial conflict with that of the Circuit Court of Appeals for the Seventh Circuit in *Swanson* v. *Commissioner,* 76 F. (2d) 651, in which writ of certiorari was applied for June 7, 1935, No. 108, October Term, 1935, and the Government is not opposing the taxpayer's petition.

Wherefore, it is respectfully submitted that this petition should be granted.

STANLEY REED,
Solicitor General.

JULY 1935.

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